

Business on the Frontline

By John Mauldin | August 21, 2020



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I write this introduction from an all-too-short vacation in Montana (more below). This week I have asked my longtime associate Patrick Watson to step in and write *Thoughts from the Frontline*, offering his perspective as a small business owner.

As you read this, realize his story is being played out hundreds of thousands of times all over the US and maybe millions of times all over the world. It is why I said last week that this depression/recession is unlike any we have experienced. Parts of our economy are doing well, parts are in recession, and a significant portion is already in a depression. As government guarantees wane in the future, more and more companies and people will slip into the depression category. But I will let Patrick tell his own story.

Patrick initially came to work for me in the late 1980s. He has worked off and on for my numerous businesses over the years while also pursuing other ventures of his own. Now he helps me each week with *Thoughts from the Frontline* research, as well as being the lead collaborator for *Over My Shoulder*. His summaries at the beginning of each issue have become very popular. He has a real talent for that.

For good or ill, he also has the dubious distinction of having read and edited more of my words than anyone over the past 30+ years. I have come to rely upon his candor and insights. He has sharpened my writing and forces me to back up my assertions with facts. He makes my work even better and I am truly grateful. I think you'll find his story enlightening.

Small Business in a Pandemic

By Patrick Watson

Like many people nowadays, I have two jobs. They are in radically different fields. The Mauldin Economics part of my life keeps me buried in economic research and financial news. I'm on the phone with John almost every day, trading information as we produce *Thoughts from the Frontline* and *Over My Shoulder*. At the same time, I co-own a small business that's plugged into a local community and serves people up close, in person.

I once heard someone say you've beaten the odds if your small business is still open after five years, profitably or not. If so, then my wife Grace and I did something right. We opened a hair salon in 2002 in Lakeway, Texas. We're still in business now though, as you will see, a lot has changed recently.

We were a good team to start this business. She'd been doing top-level hair design for 20+ years. I had a few financial and marketing skills. We named it "Transformation" because change was our specialty. COVID-19 was a change we didn't expect. It made my two careers collide.

This was beneficial in some ways. My micro-level experience gave John useful information as he helped readers navigate the macro-level economic crisis. So, this week we decided to give you a deeper look. I hope, after reading this, you'll see the economic data in a different way. It isn't just charts and numbers. It's about real people having their lives turned upside down.

Because I watch the economic news and saw what happened in China and then Italy, we acted early in February to enhance our already-high salon hygiene standards. We made some physical changes to simplify cleaning and looked (unsuccessfully) for medical-grade protective gear.

On the financial side, I started to build cash reserves and confirm our credit lines in case sales dropped. Normally, the hair business is highly predictable. People who care about their appearance get a haircut and (for older folks) hair color every 4–5 weeks. At a high-end salon like ours, they make reservations months in advance. We know pretty closely what revenue should be. So, when it slipped a little in late February then dropped more in early March—well before the local shutdown orders—we knew something serious was coming.

This confirmed what simple logic had told me to expect. Viruses spread until something stops them. We knew what this one was doing elsewhere and there was no reason to think it would act differently here.

On March 16, Grace and I decided closing the salon was our only choice. Hair styling requires extended close contact—a factor that had drawn me to the industry years earlier. It was a service that couldn't be outsourced to Asia. But now a virus *from* Asia was making that kind of contact hazardous. We didn't want to be part of making anyone sick. We also figured local authorities would order closures soon anyway (which they did, a week later), and felt it was better to do it on our own terms.

Temporary, We Thought

Closing the doors presented a financial issue: how to make payroll with no revenue. We had enough cash to cover everyone's normal pay for a while. We also knew Congress was talking about disaster relief plans, though nothing had passed yet.

In cold business terms, we should have immediately laid off everyone, but our little team (all nine of us) was like family. We also had to think about the future, preserving our cash and credit for tough conditions when we reopened in a weak economy. We dug into savings to pay everyone for the rest of March while looking for better ideas.

About that time, Congress passed the Paycheck Protection Program. I knew, however, its funding was limited and essentially every small business (and some not-so-small ones) could meet the vague requirements. Our longtime bank filed our PPP application the second day the program opened. That turned out to be too late. The available funding got snapped up almost immediately... and we had payroll coming due.

We could either keep paying everyone out of pocket, burning through liquidity we would need later, or make temporary layoffs. That was a hard choice, but we stressed to everyone how we fully intended to reopen when possible. All this was going to be temporary, we thought. Meanwhile, the enhanced unemployment benefits were enough to keep everyone afloat.

Grace went to work planning exactly how we would reopen. That was a challenge because the rules seemed to change daily. She collected three huge binders of guidance from different agencies and professional organizations. All were trying to be helpful but the often conflicting suggestions and requirements just added to our uncertainty.

The background news by that point was all about New York, where hospitals were filling and thousands dying. Nothing like that was happening where we are in Texas, but we knew it might be coming. We told customers we would reopen when two conditions were met.

- We were legally allowed to open, *and*
- We believed we could operate safely.

The second point had both micro and macro levels. We would need to do certain things in the salon *and* know conditions in our area wouldn't render them moot. But how to measure that?

I thought the [Opening Up America Again](#) plan the White House released on April 16 made sense. It had specific criteria to meet before reopening, including a 14-day decline in new cases. That became our guidepost. I didn't foresee that the White House and our own governor would soon ignore the plan.

About that time is when anti-lockdown protests began spreading around the country. I understood how people were frustrated, and many were suffering economically. I didn't get the complaints about non-essential things. As a hair salon owner, I think what we do is important, but not important enough to justify endangering public health. Yet that whole time, we were getting daily phone calls from people desperately wanting illegal haircuts. Some offered large amounts of money. We politely declined.

Nevertheless, the discontent had a political effect. On April 27, with virus cases still *rising* in Texas, Gov. Greg Abbott announced a phased reopening would begin May 1. (Why he ignored the White House criteria, I still don't know. I guess he had reasons.) The initial phase didn't include hair salons but Abbott said they would look at allowing salons to open in "mid-May." That wasn't great news to us, but it helped to know what to expect.

Then on May 5, Abbott announced at a hastily called press conference hair salons could open on May 8 instead of mid-May as he had hinted just days earlier. The urgency still puzzles me. Grace and I knew we couldn't reopen that quickly, especially since Texas regulators would no doubt be issuing new requirements we hadn't even seen yet.

More than Hair

On the first day Texas salons could reopen, I drove around to see what was happening. Top-tier salons like ours looked mostly still closed. So were some of the inexpensive "chop shops" that sell quick haircuts. But at one I saw about a dozen shaggy-headed males waiting outside. None were wearing masks (which weren't required at that point) and they were standing well within six feet of each other. I didn't go inside but I could guess the scene: overwhelmed stylists with subpar protective gear, risking their own health.

As we thought through all this, safety and financial factors started to overlap. Just as restaurants make money by "turning tables," the salon business depends on having your chairs deliver a certain amount of revenue per hour. Anything that slows down the process hurts, and the new cleaning and capacity requirements were a big problem.

Running the numbers, it was pretty clear we couldn't maintain our level of quality and make a profit. The virus—and the measures to control it—had killed our business model.

There was more, too. We didn't do quick cuts; we made people look and *feel* beautiful, in a relaxed and comfortable atmosphere. Our stylists did highly customized, precision work and we charged accordingly. That was now going to be much harder. Breakeven was the *best*-case scenario. Profit? Out of the question.

We started getting stories from industry colleagues. Some stylists, especially the young ones, were just happy to be back at work. Others told us they were miserable. Communication with masks was difficult, causing misunderstandings. The normal banter and conversation were impossible. It just wasn't fun anymore.

Then there was the mask problem. People would try to enter salons without masks, or leave their noses uncovered, causing ugly scenes. I didn't want our team having to be the Mask Police—especially since the real police had been made powerless to help. That was frustrating.

One salon in our area endured disaster. A customer who had been sick and was awaiting COVID test results simply lied on the screening questionnaire. Then, *while* she was in the salon getting color, she got a phone call telling her the test was positive. The salon had to close for two weeks while the entire staff isolated—a huge financial hit.

In the middle of all this, we finally got approved for a PPP loan. It would have let us reopen for a few weeks. But then what? As hard as we tried, we couldn't see a safe, sustainable recovery path.

For me personally, there was something else. Reopening the salon wasn't just a business decision; it would mean sending my wife into danger. That didn't feel good. We had employees and many customers with various health issues, too. The thought that we might spread this sometimes-deadly virus and hurt one of them was unbearable.

The final straw came when one of our longtime stylists was offered another professional opportunity, the kind he couldn't turn down. We were excited for him and still are, but it changed our already-bad outlook for the worse. Finding a replacement while also dealing with all the other issues would have been risky and difficult.

At that point, Grace and I knew the business had to either close permanently or evolve into something different. We decided to evolve.

A Way Forward

Our work at Transformation has always been about more than money. We cared about our guests from head to toe. We walked with many cancer patients through the agony of losing their hair. We were there for countless graduations, weddings, anniversaries, and funerals. I think the refuge we provided probably preserved some marriages. I know we averted at least one suicide. That mission had to go on in some way.

Looking at this new world, we realized some things *haven't* changed. People still want quality hair care, if they can get it safely. They still want connection and community. And now, they want to escape from this crazy new world, if only for a little while.

Grace and I live in the Texas Hill Country outside Austin. We own another small house near our home. Our salon lease had run out in the middle of all this, and we realized that little building could be a new salon. It is a beautiful, secluded location where we can serve people safely, one or two at a time, far from crowds. There's a natural area where we are building some meditation spaces, and a concrete pad we'll use for outdoor yoga and wellness treatments. It will be nothing like the bustling, high-energy salon we ran for the last 18 years, but we'll still help people and create a few new jobs.

I hope that's how the rest of the economy develops. Technology and other changes have been killing whole industries for many years. That's nothing new. The difference this time is the speed with which it happened to restaurants, bars, hotels, airlines, and others for which personal proximity is part of the product. We are among the lucky ones with the means to pivot in a new direction. Many can't, and the assorted aid programs like PPP were too little, too complicated, and too late. But I'm not sure anything else would have been better.

I think our business will survive largely because we had better information. The closure didn't shock us, as it did many others. We were as ready as anyone could be. Most small businesses weren't ready, are now badly damaged, and may never recover. Their workers will stay jobless while their lenders and landlords face certain losses. I agree with the "depression" call John made last week. Sadly, I see no way out of it.

Let me close by thanking John for giving me the keyboard this week. I hope this story helps show you how this crisis unfolded at ground level. If you're a small business owner wrestling with hard choices, you can reach me through [Mauldin Economics customer service](#). To get more of my thoughts on the economy, [subscribe to *Over My Shoulder*](#).

Ok, John back now. I get a private email from a professor at a well-known university in England (I don't have permission to share his name). It documents COVID research from everywhere, running 20–30 pages every day. It often has conflicting data, but he chronicles it nonetheless. Randomly, this paragraph on hair salons showed up yesterday:

Another report from investigators in Missouri found that adherence to universal masking for source control as mandated by city ordinance and company policy helped prevent transmission of SARS-CoV-2 from 2 symptomatically infected stylists at a hair salon in Springfield, Missouri. Before they were diagnosed as having COVID-19, the hair stylists had served 139 clients but had been required to wear masks at all times while working with them. After public health contact tracing with the hair salon clients and after 2 weeks of follow-up, no symptoms of COVID-19 were identified among the exposed clients or their secondary contacts. Among 104 interviewed clients, 102 (98%) reported wearing face coverings for their entire appointment...

It appears Patrick was correct in his concerns. He and I talked several times a week as he experienced all this. I talk to other small business owners all over the country, just wanting to know what is happening on the ground. Almost all report the same agony of caring for employees, customers, and what they will do. The pressure is so very real.

To think that this is not going to change the character and psyche of our nation and world, to affect our decisions and habits, our views about family, community, and government, is simply ludicrous. The open question, however, is how?

And as the Fourth Turning, the geopolitical Storm Before the Calm, and The Great Reset all collide in this decade, along with the Age of Transformation? Not only is everything going to be repriced, our society and our relationship with what we think of as nation-states will be transformed.

It is our duty not to see those whose ideas are different as partisan enemies, lumping them into some kind of sub-human species, but to try and move forward to manage the transformation into a better world.

We must find common ground, a new middle, a way of less anger and strife—or this decade will not be one of peace, but of violence. There is so much promise. I see it. The transformation is going to happen. I hope it will not have to be from the rubble but from a shared sense of community.

I still believe the best bet is to be long humanity and short government.

Montana and Puerto Rico

I write from Darrell Cain's kitchen table, looking over a glass-smooth Flathead Lake in Montana, surrounded by thousands of flowers and scores of hummingbirds. Shane and I have to leave this idyllic home tomorrow to go back to our own slice of paradise. I am such a blessed human being, although this year's lack of travel is making me a little stir-crazy.

Randomly, my daughter Tiffani and a friend were traveling through the area on their way to Whitefish and have stayed the night. Darrell is a banana bread lover, and Tiffani and I will make my mother's recipe for banana bread cake (and icing), which is still the best I have ever had anywhere.

I have been reading a lot here. And thinking, maybe worrying a little more about the future than I should. But the Republic has survived worse than we have today, and the technological future has never been brighter. And the smell of baking banana bread cake is wafting through the kitchen, so maybe I should worry less and live in the moment more.

Have a great week and call your friends and share some moments. It will make your world better.

Your wanting another week somewhere analyst,



John Mauldin

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